

### Direct Rollover to a Traditional IRA

If you want your payment made directly to a traditional IRA, contact the financial institution where you opened the IRA to find out how you can transfer your payment. If you roll your after-tax contributions to a traditional IRA, it is your responsibility to report the amount of after-tax contributions to the IRS. Be sure the IRA you choose will allow you to move all or part of your payment to another IRA at a later date without penalties or other limitations. (See IRS Publication 590, "Individual Retirement Arrangements").

### Direct Rollover to a Qualified Employer Plan

If you go to work for a new employer that has a qualified employer plan, ask your employer whether they will accept your direct rollover. If they don't, you can choose a direct rollover to an IRA instead. A qualified employer plan is not legally required to accept a rollover.

### PAYMENTS MADE TO YOU

If you choose to have the payment made to you, it is subject to a 20% federal income tax withholding. The payment is taxed in the year you receive it, unless you roll it over to an IRA or a qualified employer plan that accepts rollovers within 60 days after receiving it. If you don't roll it over, special tax rules may apply.

### Mandatory Tax Withholding

If your payment is eligible for a rollover and you choose not to rollover your lump sum payment, SERS is required by federal law to withhold 20% of the taxable amount. This money is then sent to the IRS as income tax withholding. For example, if the taxable portion of your eligible rollover payment is \$10,000, only \$8,000 will be paid to you because SERS must withhold \$2,000 as income tax. However, when you prepare your income tax return for that year, you report the \$2,000 as tax withheld, and it will be credited against any income tax you owe.

### Sixty-Day Rollover Option

If you do not ask SERS to transfer the payment directly to another qualified plan, 20% of the taxable payment will be withheld as federal income tax and the balance will be mailed to you. Once you receive payment, you can still decide to roll over all or part of your lump sum payment to a qualified plan within 60 days of receiving the payment. The amount you rollover will not be taxed until you withdraw it. You can rollover up to 100% of your eligible payment, including the 20% that was withheld as taxes, but

you must find other money to replace the 20% that SERS withheld for taxes. If you rollover the 80% you received, you will only be taxed on the 20% that SERS withheld.

### Additional 10% Excise Tax on Distributions Before Age 55

A refund of contributions following severance of employment before age 55 (50 for police positions) is subject to a 10% excise tax if you do not roll it over. The excise tax does not apply to a refund of contributions following severance of employment after age 55, or from death or disability.

### SURVIVING SPOUSE - ALTERNATE PAYEE - OTHER BENEFICIARY

In general, the rules that apply to payments to members also apply to payments to their surviving spouse. Some of the rules described above also apply to a deceased member's beneficiary who is not a spouse. If you are a surviving spouse, alternate payee or beneficiary, you can have your payment rolled over, paid in a direct rollover to a traditional or simple IRA or qualified employer plan, or have it paid to you. If you have the payment sent to your home, you can keep it or roll it over yourself into a plan that accepts rollovers.

If you are a surviving spouse, alternate payee or other beneficiary, your payment is generally not subject to the additional 10% excise tax. You may also be able to use the special tax treatment for lump sum distributions as described in IRS Publication 575, Lump-Sum Distributions.

### OBTAINING ADDITIONAL INFORMATION

This brochure summarizes the federal tax rules that may apply to your lump sum payment. You can find more specific information on the tax treatment of lump sum payments from qualified retirement plans in IRS Publication 575 "Pension and Annuity Income," and IRS Publication 590 "Individual Retirement Arrangements." These publications are available from your local IRS office, on the IRS's web site at [www.irs.gov](http://www.irs.gov), or by calling 1-800-TAX-FORM.

**Note – Please note that benefits or lump sum resignation refunds are not paid unless they are requested and the appropriate forms are completed and submitted to SERS.**



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**SRS** State Employees'  
Retirement System

# TAXES, LUMP SUM PAYMENTS & ROLLOVERS



The State Employees' Retirement System (SERS) is a qualified plan under Section 401(a) of the Internal Revenue Code. This brochure presents the possible tax consequences on SERS benefits. SERS staff are not experts on the tax code so please contact the Internal Revenue Service, or your tax advisor regarding your tax liability and the preparation of tax returns.

## TAXES

In this brochure, for tax purposes, the term “employee contributions” generally refers to:

- Contributions made to SERS prior to January 1, 1982. These contributions were made on an after-tax basis.
- Contributions and interest paid on an after-tax basis for optional service purchases.

## ILLINOIS STATE INCOME TAX

All SERS benefits are exempt from state income tax under Illinois law.

## FEDERAL INCOME TAX

### Annual Tax Statement – Form 1099-R

The Illinois Office of the Comptroller will send you a 1099-R tax statement every January. This information should be used for filing your federal and state income tax returns.

### Federal Income Tax Withholding for Monthly Payments

Other than monthly occupational disability benefits and monthly occupational death benefits, all monthly payments made by SERS are subject to federal income tax withholding in accordance with Federal Withholding Tables. When you apply for a benefit, you will elect how you want federal taxes withheld.

You may elect not to have withholding taken, or to have withholding taken at any level. If you do not indicate a preference for withholding, federal taxes are withheld at the rate for a married person with three exemptions. You may change your withholding or discontinue withholding at any time.

### Taxation of a Retirement Annuity

Pension payments are subject to federal income tax under the Simplified Method. This method states that a portion of each benefit payment is taxable, and a portion is non-taxable based on the recovery of employee contributions and the age of the individual. Following the recovery of the employee contributions, the entire gross benefit payment becomes taxable.

The amount of the monthly benefit that is non-taxable (if any) will be provided when the benefit begins. If you die with no eligible survivor or nominated beneficiary to receive any death benefits that may be payable, any remaining employee contributions may be claimed as a miscellaneous itemized deduction (not subject to the 2% floor) on your final tax return.

### Taxation of Disability Benefits

Occupational disability benefits paid by SERS are exempt from federal tax. Although exempt, these benefits are reportable and a Form 1099-R will be issued each January.

Non-occupational disability and temporary disability benefits are subject to federal income tax; therefore, a form 1099-R will be issued each January.

### Taxation of Survivor Benefits

The monthly benefit paid to a survivor, as well as the \$1,000 lump sum survivor benefit is subject to federal income tax under the Simplified Method. This method states that a portion of each payment is taxable, and a portion is nontaxable based on the recovery of employee contributions and the annuitant's age. Following the recovery of the employee contributions, the entire gross benefit becomes taxable including any increase to the benefit. Following the death of the survivor, if there is not an eligible nominated beneficiary to receive any death benefits that may be payable, any remaining employee contributions may be used as a deduction on the final tax return of the survivor. The amount of the monthly benefit that is non-taxable will be provided to the survivor when the benefit begins.

### Taxation of Occupational Death Benefit

Monthly occupational death benefits are exempt from both federal and Illinois income tax.

### Taxation of State Insurance Coverage

Annuitants who cover non-IRS dependent(s) on their state health and dental insurance will receive Form W2GI+ from the Illinois Office of the Comptroller. Under federal tax law, if a covered dependent does not qualify as your tax dependent, the premium paid by the State must be added to your annual gross income and be subject to federal income tax. The W2GI+ is also issued for all annuitants who carry over \$50,000 in group term life insurance (in accordance with federal tax law).

## LUMP SUM PAYMENTS & ROLLOVERS

All lump sum payments are subject to federal income tax withholding. Withholding may be avoided in certain cases by rolling-over the lump-sum payment. You can rollover lump-sum payments to the following: 401(a) plan, 401(k) plan, 403(b) plan, eligible 457 plan, traditional IRA, simple IRA or Roth IRA (special IRS rules apply to Roth IRA).

### Lump Sum Payments Include:

- Non-occupational death benefit before retirement
- Non-occupational death benefit after retirement
- Occupational death benefit (lump sum only)
- Refund of survivor contributions
- Refund of contributions after withdrawal from service
- Alternative formula contribution refund.

These SERS taxable lump sum payments are eligible for a rollover. A direct rollover is a direct payment of the amount of your SERS taxable lump sum payment to an eligible plan that will accept the rollover. Except in the case of a rollover to a Roth IRA, you are not taxed on any taxable portion of your payment until you withdraw it from the eligible plan.

If you do not rollover your lump sum payment, the lump sum payment is subject to a 20% federal withholding rate. Your lump sum payment cannot be rolled over to an Educational IRA. The non-taxable portion (after-tax contributions) may be rolled into plans that accept rollovers of after-tax contributions. It must be a direct transfer and the plan must agree to accept the transfer and account for it separately. The non-taxable portion of your lump sum payment may not be rolled over to a 457 plan (Deferred Compensation).

**Please note that lump sum payments and rollover rules are complex and contain many conditions and exceptions that may not be included here. Therefore, you may want to consult with a professional tax advisor or the Internal Revenue Service before receiving your SERS payment.**

There are two ways to receive your lump sum payment that is eligible for a rollover:

1. The payment can be made directly to an eligible plan that will accept it; or
2. The payment can be paid to you.

**Whether you receive your payment now, or roll it over, will affect the tax you owe.**

## DIRECT ROLLOVER

In a direct rollover, your payment is transferred directly from SERS to a plan that accepts rollovers. If you choose a direct rollover, you are not taxed on your payment until you withdraw it from the eligible plan (unless you choose to rollover into a Roth IRA). You can choose a direct rollover of all or any portion of your taxable payment.